

CHAPTER 3B

CIGARETTE AND TOBACCO PRODUCTS TAX

HIGHLIGHTS

- Tax Base Cigarettes and other tobacco products.
- Rate Cigarettes: \$0.87 per pack.
Other tobacco products: 45.13% of the wholesale cost of tobacco, effective July 1, 2008 through June 30, 2009. The other tobacco products tax rate is updated annually each July 1.
- Revenue

2007-08 (Actual)	\$1.0 billion
2008-09 (Estimate)	\$1.0 billion*
2009-10 (Estimate)	\$1.0 billion*

1.1% of all state revenues
- Administration Board of Equalization (BOE)

*General Fund revenue is estimated to be \$113 million and \$111 million

1. TAX OVERVIEW

California levies two distinct excise taxes on tobacco products: the cigarette tax and the tobacco products tax that is imposed on items such as cigars, pipe tobacco, and chewing tobacco. Both excise taxes are imposed on distributors but ultimately passed on to consumers.

Tobacco taxes incorporated into the retail price of tobacco products become part of the sales tax base for those products.

2. TAX RATE

Prior to 1989, California levied an excise tax of five mills (\$0.005) on each cigarette, or \$0.10 on each pack of 20 cigarettes.

Passage of Proposition 99 in November 1988 increased the excise tax on cigarettes by \$0.25 per pack (to \$0.35 per pack) effective January 1, 1989 and imposed a “tobacco products tax” on cigars, chewing tobacco, pipe tobacco, and snuff. The tobacco products tax, which is stated as a percentage of the wholesale cost of tobacco, was set at a rate

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equivalent to the excise tax on cigarettes. Proposition 99 revenues are deposited into the Cigarette and Tobacco Products Surtax Fund to support anti-smoking education programs, tobacco-related diseases research, indigent health care and public resources.

An additional \$0.02 per pack cigarette increase was added in 1994 to fund Breast Cancer Research. The proceeds from the tax are deposited in the Breast Cancer Fund, with allocations to the Breast Cancer Research Program and the Breast Cancer Control Program.

Passage of Proposition 10 in November 1998 further increased both the cigarette and tobacco products tax rates. Pursuant to Proposition 10, the cigarette tax rate increased by \$0.50 per pack and the other tobacco products tax rate increased by an equivalent amount, effective January 1, 1999. Proposition 10 requires that revenues from the Proposition 10 tax increase be deposited in the California Children and Families First Trust Fund for the purpose of promoting, supporting, and improving the development of children from the prenatal stage to five years of age.

Proposition 10 also indirectly generated a second increase in the other tobacco products tax rate, beginning July 1, 1999. This additional increase resulted because Proposition 99 requires the other tobacco products tax rate to be recalculated on July 1 of each year based on the wholesale price of cigarettes in March of that year. Thus, when Proposition 10 increased the tax on a pack of cigarettes by \$0.50 on January 1, it indirectly triggered an *additional* increase in the other tobacco products tax on July 1, 1999. Revenues from this additional increase were deposited in the Cigarette and Tobacco Products Surtax Fund to fund Proposition 99 programs.

3. EXEMPTIONS

Sales of cigarettes or other tobacco products to Armed Forces exchanges, commissaries, Naval or Coast Guard ships and stores, and to the Veterans Administration are exempt from the tax, as are up to 400 cigarettes transported or brought into California by any individual for his or her personal consumption. The U.S. Constitution also exempts sales by Indian smoke shops to Indians.

4. FEDERAL TAXATION

The federal government imposes excise taxes on cigarettes and tobacco products at the following rates:

Small cigars (weighing 3 lbs. or less*)	\$1.828 per thousand
Large cigars (weighing more than 3 lbs.*)	20.719% of wholesale price, not to exceed \$48.75
Small cigarettes (weighing 3 lbs. or less*)	\$19.50 per thousand
Large cigarettes (more than 3 lbs.*)	\$40.95 per thousand
Snuff	\$ 0.585 per pound

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Chewing Tobacco	\$ 0.195 per pound
Pipe Tobacco	\$ 1.0969 per pound
* Per thousand	

These federal excise taxes are imposed in addition to state excise taxes and are included in the state sales tax base.

5. REVENUE

Total tobacco tax revenues for the 2006-07, 2007-08 and 2008-09 fiscal years are shown below:

	2006-07 (\$ Millions) <u>actual</u>	2007-08 (\$ Millions) <u>actual</u>	2008-09 (\$ Millions) <u>estimate</u>	2009-10 (\$ Millions) <u>estimate</u>
General Fund	\$115.4	\$109.8	\$113.0	\$111.0
Cigarette and Tobacco Products Surtax Fund (Proposition 99)	335.9	327.0	315.0	310.0
Breast Cancer Fund	27.3	22.0	23.0	22.0
California Children and Families First Fund (Proposition 10)	603.4	576.7	581.0	570.0

Use of Special Funds. Cigarette and Tobacco Products Surtax (Proposition 99) Fund:
Money in the Cigarette and Tobacco Products Surtax Fund is allocated in the following ways:

- Health Education Account 20% for education on the prevention and reduction of tobacco use
- Hospital Services Account 35% to pay hospitals for the treatment of indigent, uninsured patients
- Physicians Services Account 10% to pay physicians who render medical services to indigent patients
- Research Account 5% to fund research on tobacco-related diseases
- Public Resources Account 5% to be equally divided between wildlife preservation programs and

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improvement of state and local park
and recreation facilities

- General Purposes (Unallocated Account) 25% to be used for any of the
specific purposes described above

Barring any revenue offsets, Proposition 10 would be expected to result in a decrease in revenues to the Cigarette and Tobacco Products Surtax Fund. This decrease would result from an overall reduction in sales of cigarettes and other tobacco products. However, Proposition 10 requires BOE to determine the fiscal effect of the decrease in consumption on any Proposition 99 state health-related education or research programs and Breast Cancer Fund programs. To the extent these programs lose money as a result of Proposition 10, Proposition 10 requires that funds be transferred from the Children and Families First Fund to the Proposition 99 and Breast Cancer Funds to backfill the losses.

This backfill provision does not extend to Proposition 99 health care or public resources programs.

Breast Cancer Fund: As noted earlier, revenue in the Breast Cancer Fund is directed toward research into the cause, cure, treatment, early detection, and prevention of breast cancer. The money in the Breast Cancer Fund is divided equally between two accounts: the Breast Cancer Research Account and the Breast Cancer Control Account.

The Breast Cancer Research Account shall allocate 10% of its moneys for the collection of breast cancer-related data and 90% of its moneys to the Breast Cancer Research Program created at the University of California to award grants and contracts for research related to the cause, cure, treatment, prevention, and earlier detection of breast cancer. The Breast Cancer Control Account shall allocate its moneys to provide early breast cancer detection services for uninsured and underinsured women.

California Children and Families First (Proposition 10) Fund: Proposition 10 creates one state commission and authorizes the creation of 58 local commissions (one in each county) to carry out the purpose of the proposition. After the Proposition 99 and Breast Cancer Funds are backfilled to alleviate certain losses they experience as a result of Proposition 10, 20% of the remaining funds are allocated to the state commission and 80% to the local commissions. The 20% allocated to the State commission funds must be spent for the following purposes:

- Mass Medical Communications 6%/20% to a Mass Media
Communications Account for
television, radio, newspaper, and
other mass media communications
that relate to and further the goals of
the act related to early childhood

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development.

- Education
5%/20% to an Education Account for development of educational materials, professional and parental education and training, and technical support for county commissions.
- Child Care
3%/20% to a Child Care Account for programs related to the education and training of child care providers and the development of educational materials and guidelines for child care workers.
- Research and Development
3%/20% to a Research and Development Account to fund early childhood development research and evaluation of early childhood development programs and services that are established pursuant to the proposition.
- Administration
1%/20% for administrative expenses of the state commission.
- General Purposes
2%/20% to be used by the state commission for any of the purposes of the proposition.

Each local commission is required to develop a strategic plan for supporting and improving early childhood development in its county and to spend its Proposition 10 funds in a manner consistent with its strategic plan. The formula for allocating revenues to the county commissions is based on the annual number of births in each participating county.

6. ADMINISTRATION

The BOE is the state agency responsible for collecting the cigarette and tobacco products tax. The cigarette tax is collected from distributors, who purchase stamps to affix to each pack of cigarettes.

Licensed distributors are allowed a discount of 0.85% of the value of the stamps at the time of purchase. This discount is designed to help offset the costs of affixing the stamps to each pack of cigarettes.

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Criminal penalties apply to forging tax stamps or for possessing, keeping, storing or retaining for the purpose of sale or for selling or possessing for sale counterfeit cigarettes or tobacco products.

Cigars, pipe tobacco, snuff, and chewing tobacco are not stamped. The taxes on the tobacco products are collected from distributors based on the wholesale cost of the tobacco products.

7. CODE

Revenue and Taxation Code Sections 30001-30481

Revenue and Taxation Code Sections 30473.5, 30474, 30474.1